

**MARYLAND CORRECTIONAL ENTERPRISES**  
**(An Enterprise Fund of the State of Maryland)**

**Financial Statements Together with**  
**Report of Independent Public Accountants**

**For the Years Ended June 30, 2013 and 2012**



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**JUNE 30, 2013 AND 2012**

**TABLE OF CONTENTS**

<b>REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS</b>	<b>1</b>
<b>MANAGEMENT'S DISCUSSION AND ANALYSIS</b>	<b>3</b>
<b>FINANCIAL STATEMENTS</b>	
Statements of Net Position	11
Statements of Revenue, Expenses, and Change in Net Position	12
Statements of Cash Flows	13
Notes to the Financial Statements	14
<b>SUPPLEMENTAL SCHEDULES</b>	
Schedules of Cost of Sales and Services	23



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## REPORT OF INDEPENDENT PUBLIC ACCOUNTANTS

The Honorable Gary Maynard, Secretary  
Department of Public Safety and Correctional Services

### **Report on the Financial Statements**

We have audited the accompanying financial statements of Maryland Correctional Enterprises (MCE), an enterprise fund of the State of Maryland as of and for the years ended June 30, 2013 and 2012, and the related notes to the financial statements, as listed in the table of contents.

### ***Management's Responsibility for the Financial Statements***

MCE's management is responsible for the preparation and fair presentation of these financial statements in accordance with accounting principles generally accepted in the United States of America; this includes the design, implementation, and maintenance of internal control relevant to the preparation and fair presentation of financial statements that are free from material misstatement, whether due to fraud or error.

### ***Auditor's Responsibility***

Our responsibility is to express an opinion on these financial statements based on our audit. We conducted our audit in accordance with auditing standards generally accepted in the United States of America. Those standards require that we plan and perform the audit to obtain reasonable assurance about whether the financial statements are free from material misstatement.

An audit involves performing procedures to obtain audit evidence about the amounts and disclosures in the financial statements. The procedures selected depend on the auditor's judgment, including the assessment of the risks of material misstatement of the financial statements, whether due to fraud or error. In making those risk assessments, the auditor considers internal control relevant to the entity's preparation and fair presentation of the financial statements in order to design audit procedures that are appropriate in the circumstances, but not for the purpose of expressing an opinion on the effectiveness of the entity's internal control. Accordingly, we express no such opinion. An audit also includes evaluating the appropriateness of accounting policies used and the reasonableness of significant accounting estimates made by management, as well as evaluating the overall presentation of the financial statements.

We believe that the audit evidence we have obtained is sufficient and appropriate to provide a basis for our audit opinion.

### ***Opinion***

In our opinion, the financial statements referred to above present fairly, in all material respects, the financial position of MCE as of June 30, 2013 and 2012 and the changes in financial position thereof for the years then ended in accordance with accounting principles generally accepted in the United States of America.



SB & COMPANY, LLC

***Other Matter***

***Required Supplementary Information***

Accounting principles generally accepted in the United States of America require that the management's discussion and analysis as listed in the accompanying table of contents be presented to supplement the basic financial statements. Such information, although not a part of the basic financial statements, is required by the Governmental Accounting Standards Board who considers it to be an essential part of financial reporting for placing the basic financial statements in an appropriate operational, economic, or historical context. We have applied certain limited procedures to the required supplementary information in accordance with auditing standards generally accepted in the United States of America, which consisted of inquiries of management about the methods of preparing the information and comparing the information for consistency with management's responses to our inquiries, the basic financial statements, and other knowledge we obtained during our audit of the basic financial statements. We do not express an opinion or provide any assurance on the information because the limited procedures do not provide us with sufficient evidence to express an opinion or provide any assurance.

***Other Information***

Our audit was conducted for the purpose of forming opinions on the financial statements that collectively comprise MCE's basic financial statements. The accompanying schedules of cost of sales and services are presented for purposes of additional analysis and are not a required part of the basic financial statements.

The schedules of cost of sales and services are the responsibility of management and were derived from and relates directly to the underlying accounting and other records used to prepare the basic financial statements. Such information has been subjected to the auditing procedures applied in the audit of the basic financial statements and certain additional procedures, including comparing and reconciling such information directly to the underlying accounting and other records used to prepare the basic financial statements or to the basic financial statements themselves, and other additional procedures in accordance with auditing standards generally accepted in the United States of America. In our opinion, the schedules of cost of sales and services are fairly stated, in all material respects, in relation to the basic financial statements as a whole.

Hunt Valley, Maryland  
September 24, 2013

*SB & Company, LLC*

# **MARYLAND CORRECTIONAL ENTERPRISES**

## **Management's Discussion And Analysis June 30, 2013 and 2012**

### **GENERAL**

The following information, prepared as of September 24, 2013, should be read in conjunction with the audited consolidated financial statements of Maryland Correctional Enterprises (MCE) for the fiscal years ended June 30, 2013 and June 30, 2012.

### **FINANCIAL HIGHLIGHTS**

Revenue totaled \$50.8 million for the year ended June 30, 2013 which is a 4.2% decrease compared to last year's \$53.0 million and an increase of 0.39% compared to 2011. The decrease is a result of a tough fiscal climate with budget cuts and freezes in spending in the governmental sector.

### **OVERVIEW OF THE FINANCIAL STATEMENTS**

The statement of net position and the statement of revenue, expenses, and changes in net position report information about MCE and its activities. These statements include all assets and liabilities using the accrual basis of accounting, reporting income in the year earned and expenses in the year incurred, which is similar to accounting used by most private sector companies. The two statements report MCE's net assets and changes. The difference between assets and liabilities is one way to measure MCE's financial health, or financial position. Over time, increases or decreases in MCE's net assets is one indicator of whether its financial health is improving or declining. Consideration of other non-financial factors, however, such as changes in product lines and the availability of capital projects is necessary to assess the overall health of MCE.

The statement of cash flows is presented using the direct cash flow method. This statement provides useful information regarding the sources and uses of cash and the resulting increase or decrease in MCE's cash balances.

The notes to the financial statements provide additional information that is essential to a full understanding of the data provided in the financial statements. The notes to the financial statements can be found later in this report.

### **NET POSITION**

As mentioned earlier, net position may serve as a useful indicator of whether the financial position of MCE is improving or declining over time. Total assets decreased by \$0.1 million from \$37.5 million in 2012 to \$37.4 million in 2013. Total assets increased by \$0.2 million from \$37.3 million in 2011 to \$37.5 million in 2012.

# MARYLAND CORRECTIONAL ENTERPRISES

## Management's Discussion And Analysis June 30, 2013 and 2012

### NET ASSETS (continued)

Current assets make up the largest portion of net assets and are comprised mainly of \$15.1 million in cash, \$4.8 million in amounts due from customers, and \$10.5 million in inventories of raw materials, work-in-process and finished goods. In 2012, current assets were comprised of \$13.2 million in cash, \$5.7 million in amounts due from customers, and \$10.7 million in inventories of raw materials, work-in-process and finished goods.

MCE is 100 % self supporting and does not receive general funds from the State of Maryland. As a result, MCE must provide funding for its own equipment, vehicles and expansion programs; MCE has internally restricted the use of \$6.3 million for specific designated uses as follows:

Vehicles	\$ 685,235
Equipment	1,634,262
Expansion of current or future plants or programs	<u>3,960,960</u>
<b>Total</b>	<b><u>\$ 6,280,457</u></b>

The following analysis focuses on the net assets and changes in net assets for MCE's activities:

	Net Assets As of June 30,		
	2013	2012	2011
Current assets	\$ 30,547,473	\$ 29,741,633	\$ 28,888,414
Capital assets, net	6,845,031	7,774,576	8,403,139
Total Assets	<u>37,392,504</u>	<u>37,516,209</u>	<u>37,291,553</u>
Current liabilities	4,067,358	3,029,909	4,743,898
Noncurrent liabilities	549,254	568,193	576,984
Total Liabilities	<u>4,616,612</u>	<u>3,598,102</u>	<u>5,320,882</u>
Net Position:			
Invested in capital assets	6,845,031	7,774,576	8,403,139
Unrestricted	25,930,861	26,143,531	23,567,532
Total Net Position	<u>\$ 32,775,892</u>	<u>\$ 33,918,107</u>	<u>\$ 31,970,671</u>

The accompanying notes are an integral part of these financial statements.

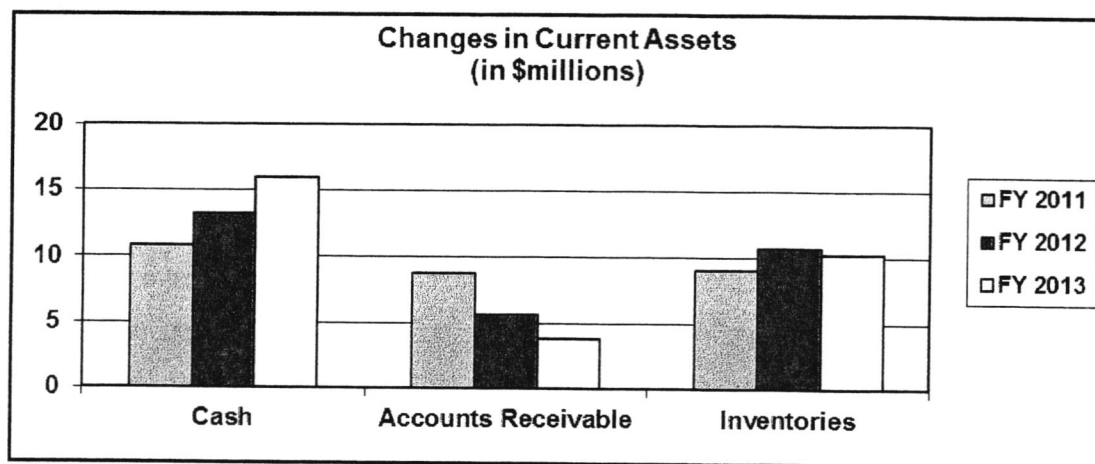
# MARYLAND CORRECTIONAL ENTERPRISES

## Management's Discussion And Analysis June 30, 2013 and 2012

### NET ASSETS (continued)

	Change in Net Position For the Years Ended June 30,		
	2013	2012	2011
Operating Revenue	\$ 50,822,528	\$ 53,026,533	50,575,354
Operating Expenses	(51,437,560)	(50,635,852)	(49,230,124)
Operating (Loss) Income	(615,032)	2,390,681	1,345,230
Non-operating Expense, net	(27,183)	(118,245)	(272,086)
Income (Loss) Before Transfers	(642,215)	2,272,436	1,073,144
Capital contributed	-	-	138,360
Transfer to State of Maryland	(500,000)	(325,000)	(376,650)
Change in Net Position	(1,142,215)	1,947,436	834,854
Net Position, Beginning	33,918,107	31,970,671	31,135,817
Net Position, Ending	<u>\$ 32,775,893</u>	<u>\$ 33,918,107</u>	<u>\$ 31,970,671</u>

Current assets increased by \$0.8 million during fiscal year 2013. This change was primarily attributable to a \$0.9 million decrease in accounts receivable, a \$1.9 million increase in cash, and \$0.2 million decrease in inventory. In fiscal year 2012 current assets increased by \$0.9 million. The change was primarily attributable to a \$3.1 million decrease in accounts receivable, a \$2.4 million increase in cash, and \$1.6 million increase in inventory.



The accompanying notes are an integral part of these financial statements.

## MARYLAND CORRECTIONAL ENTERPRISES

### Management's Discussion And Analysis June 30, 2013 and 2012

#### CAPITAL ASSETS:

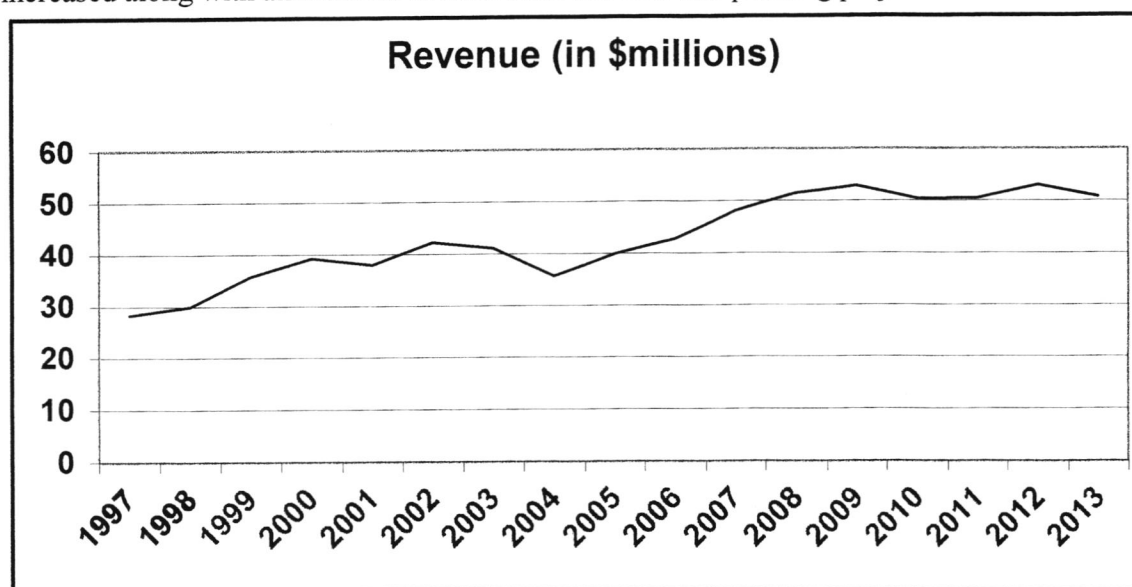
Capital assets purchased during fiscal year 2013 total \$588,000 and \$777,000 during fiscal year 2012; a decrease of \$189,000 (24%) in capital spending. Capital assets purchased during fiscal year 2012 totaled \$777,000 and \$2.6 million during fiscal year 2011; a decrease of \$1.8 million (69%) in capital spending.

#### LIABILITIES:

Total liabilities increased by approximately \$1 million during fiscal year 2013 compared to fiscal year 2012. This increase is primarily attributable to a \$0.4 million increase in accounts payable and accrued liabilities and an increase of \$0.5 million of customer deposits in the deferred revenue account. Total liabilities decreased by approximately \$1.7 million during fiscal year 2012 compared to fiscal year 2011. This decrease is primarily attributable to a \$0.9 million decrease in accounts payable and accrued liabilities and a decrease of \$0.8 million of customer deposits in the deferred revenue account.

#### OPERATING INCOME

Net operating income/loss for fiscal year 2013 is a \$0.6 million loss, a decrease of \$2.9 million from the previous fiscal year. This loss is a result of several items such as the loss of federal sales and associated profits at the Furniture Restoration plant due to federal budget cuts, reduced income in our Agricultural plant due to the completion of the Inter County Connector (ICC) tree planting mitigation project, an increase in fringe benefits and pension costs, as well as expenses associated with significantly reduced production due to inmate lock downs at the North Branch Correctional Institution Upholstery Plant. During fiscal year 2012 net operating income increased \$0.9 million from fiscal year 2011 as capital furniture projects sales to universities increased along with an increase in sales from the ICC tree planting project.



The accompanying notes are an integral part of these financial statements.

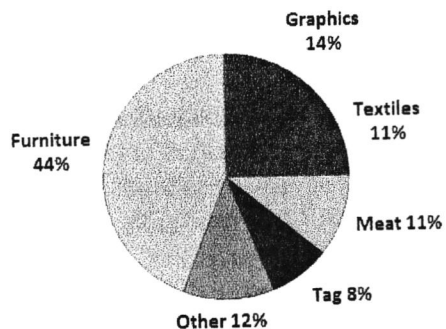


## MARYLAND CORRECTIONAL ENTERPRISES

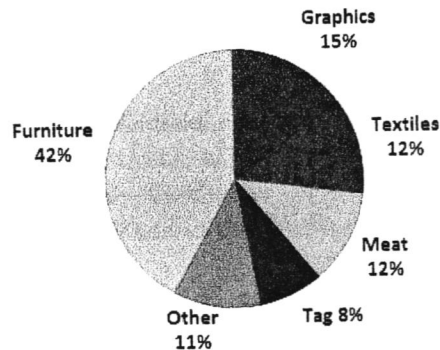
### Management's Discussion And Analysis June 30, 2013 and 2012

Shown below is a breakdown of the major revenue sources for Fiscal Years 2013 and 2012, respectively.

**Revenue Sources FY 2013**



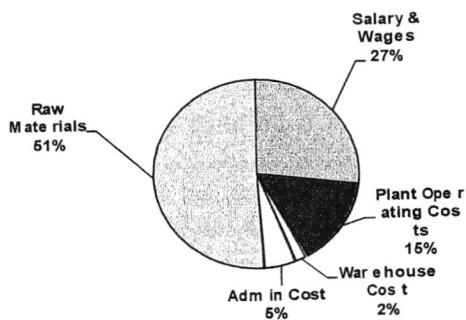
**Revenue Sources FY 2012**



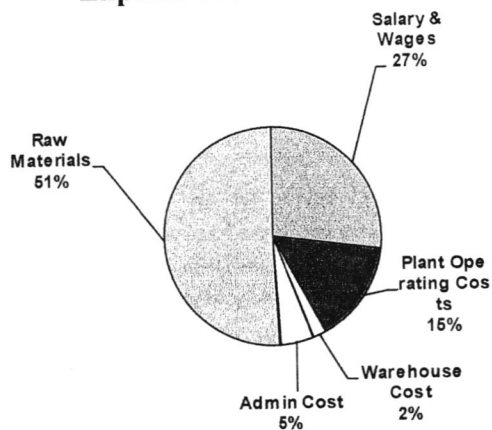
## EXPENSES

Below is a breakdown of the major expense sources for Fiscal Years 2013 and 2012.

**Expense Sources FY 2013**



**Expense Sources FY 2012**



## CURRENT OUTLOOK

MCE's revenue sources are derived mainly from governmental agencies within the State of Maryland. MCE predicts that revenue will remain relatively the same for the coming fiscal year (FY 14).

Several of MCE's cost centers do not earn revenue. For example, The CARES program (Continuing Allocation of Re-Entry Services) is a re-entry program that combines training and education to help inmates prepare for the job market when returning home. Because there is no "product or service" for sale, CARES does not generate any revenue.

The accompanying notes are an integral part of these financial statements.

## MARYLAND CORRECTIONAL ENTERPRISES

### Management's Discussion And Analysis June 30, 2013 and 2012

#### CURRENT OUTLOOK, continued

MCE has temporarily closed the new 20,000 sq. ft. MCE Upholstery Plant at the North Branch Correctional Institution effective September 2013. Institutional lock downs due to safety and security concerns shut down production due to a lack of inmate workers. Production has been transferred to the MCE Upholstery Plant at MCIH.

MCE is in the process of creating a Perpetual Inventory Control system (PICS) for the Maryland Motor Vehicle Administration (MVA) which will keep track of the inventory of license plates from the "cradle to the grave". MCE will manufacture, warehouse, maintain control over and distribute all inventories for the MVA which will increase our overall revenue.

Due to the PICS program MCE is enlarging Business Unit 113 at MCIW to accommodate the additional inventory of license plates.

The Department of General Services declared surplus the former State Surplus building plus 9.83 acres located on Brock Bridge Road in Jessup. The property was claimed by MCE and shall be transferred to MCE in as-is condition. MCE plans to renovate the building for future use for much needed warehouse space, an MCE showroom, space for the sale of MCE surplus goods, office space for MCE's sales division, and possible conference room space to be utilized by MCE's customer base. Approval was requested to transfer 9.83 +/- improved acres to the Department of Public Safety and Correctional Services. The Deed has been approved by the Office of the Attorney General. Title and transfer agreements are subject to legal review. The transfer is expected to occur on or about September 1, 2013.

MCE is currently running a test program in preparation to launch our toner remanufacturing operation which is housed in our Brush and Carton plant at MCTC in Hagerstown. In September the program will be expanded and MCE will offer sales of remanufactured toners to DPSCS units initially and then to other state agencies. Remanufactured toners are becoming an accepted way that businesses can save money and contribute to our environment while creating a savings for the state. We anticipate this business will increase our revenue, profits and inmate employment levels.

MCE is in the process of preparing a RFP for a new Enterprise Resource Planning (ERP) information system. The purpose of this project is to establish a new ERP solution that will meet the current and future needs of MCE. In order to accomplish its mission and accommodate expected growth, MCE requires a high level of financial accountability and manufacturing process insight throughout all facets of its organization. This has been increasingly difficult given the current processes (which are very paper driven) and the main computer system (which is over 15 years old). MCE's primary financial and manufacturing management system (called MAPICS now an INFOR product) provides basic accounting and customer order management services and was installed in the late 1990s.

The accompanying notes are an integral part of these financial statements.

## **MARYLAND CORRECTIONAL ENTERPRISES**

### **Management's Discussion And Analysis June 30, 2013 and 2012**

#### **CURRENT OUTLOOK, continued**

MCE was required to pay \$105,259 as of June 30, 2013 for the new State Personnel System called JobAps. We are also obligated to pay an additional \$181,000 for year 2014 and \$181,000 for year 2015.

MCE transferred \$500,000 to the State of Maryland's General Fund in June 2013 as required by the Maryland Legislature.

MCE did not propose any bills to the Legislature this year.

#### **REQUEST FOR INFORMATION**

This financial report is designed to provide a general overview of MCE's finances. Questions concerning any of the information provided in this report or requests for additional financial information should be addressed to Department of Public Safety and Correctional Services, Division of Correction, Maryland Correctional Enterprises, 7275 Waterloo Road, Jessup, Maryland 20794.